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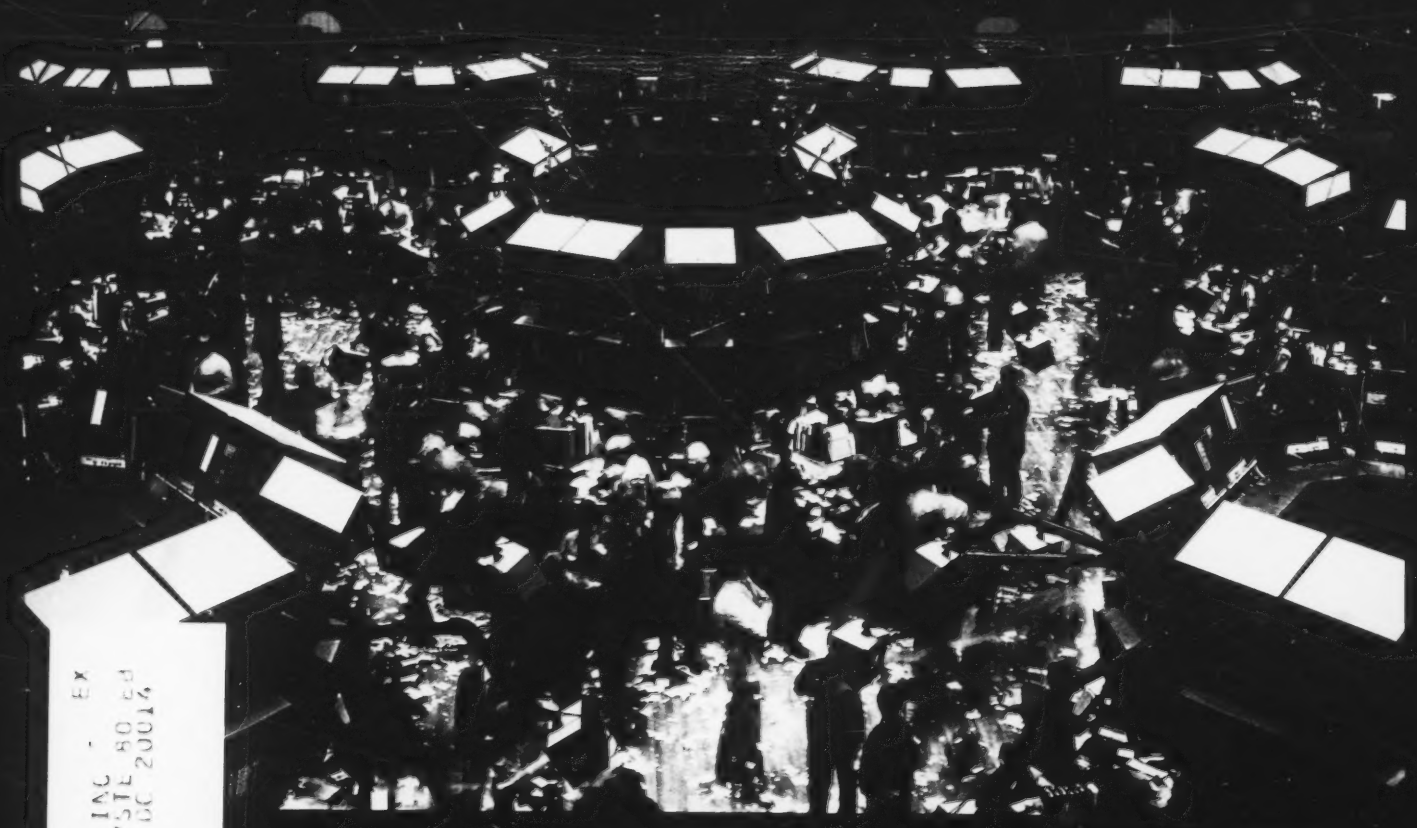
Chain Store Age EXECUTIVE

with Shopping Center Age

February 1984

The newsmagazine for retail operations



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GOING PUBLIC

Chain Store Age EXECUTIVE Volume 60, No. 2/February 1984

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Chain Store Age EXECUTIVE February 1984

A strong rally in the stock market was one factor contributing to the most advantageous market that had existed since the late 1960's.

COVER STORY

Private to public: Is the window closing?

In 1983 a record number of private companies went public. Will the market allow the trend to continue this year?

If the management of a private retail chain decided last year to take the company public, chances are the timing was right for all concerned. If it chose instead to wait, it missed the boom—and may not be so fortunate if wanting to go public this year.

The boom that happened in 1983 consisted of the largest amount of capital ever raised in a single year through initial public offerings (IPOs). Last year's $12 billion in market capitalization was four times greater than the old record of $3 billion—and equal to the total amount raised during the prior 12 years. Thirty-seven retail companies took part in the boom.

The immediate advantage for a company in going public is an increase in the amount of capital available, and thus, greater company equity. This, in turn, makes it easier to borrow money through conventional sources and additional capital can be raised through subsequent offerings. In addition, by being public, companies are able to offer stock options that help them in both attracting and retaining quality employees.

Conversely, among the disadvantages are the costs involved, including accountants' and lawyers' fees and printing expenses, all of which go up when a company goes public. Then, there are the vagaries of the stock market itself.

The greatest disadvantage, though, is that the executive in charge now has a large group of other people looking over his shoulder. Yet, given the opportunity, many executives feel going public is worth the price.

Recent IPOs can be found in almost every retail classification. The 1983 roster includes such companies as Entre Computer Centers, Dress Barn, Designhouse International, Farm Fresh, National Lumber & Supply, Crown Books, Trak Auto, Williams-Sonoma and Medicare-Glaser (*see accompanying chart*).

Companies in the fields viewed as "fast growth" areas have been particularly active—computer retailing chains (six IPOs) and off-price apparel and footwear retailers (five IPOs).

What these companies reacted to was the most advantageous market for taking a company public that had existed since the late 1960's. It had no single cause, "But rather a lot of different factors got involved," says Roger LoPata, editor of "Going Public: The IPO Reporter," a newsletter published by Howard & Co., Philadelphia.

The first factor was a strong rally in the stock market which began in August 1982, coming off a bad cycle and what had been a bad year for IPOs.

"Typically over time when there is a prolonged rally in the stock market, the perception starts in private companies that maybe they should go public. But it takes time to put the whole thing together," says LoPata.

The amount of preparation involved, including the review period by the Securities and Exchange Commission (as long as two to three months during the height of the IPO flurry), means that from the time the market picks up there is a lag of about three months. That's one reason why the real IPO surge didn't start until the beginning of 1983.

The second major factor was the interest shown by institutional investors in IPOs—particularly those of young, growth companies. (Burlington Coat Factory reports that of the approximately 40% of the company's stock offered when it went public, institutional investors gobbled up 70%.)

What happened was that during 1981 and 1982 institutional investors had invested a disproportionate amount of their money in money market funds, lured by returns of 16% to 18%.

When interest rates started com-

***Thirty-seven retail companies** took part in the "going public" boom in 1983—$12 billion in market capitalization.*

ing down, they felt pressure to move some of their monies out. Unable to find something to generate a comparable 18% cash return, "They decided if not cash, how about growth companies." Such interest was "absolutely unprecedented" and meant that "The window for IPOs opened wider with more money available than ever before to support offerings," LoPata observes.

Lastly, 1983 witnessed a change in attitude on the part of New York City's 23 financial leaders toward IPOs. Traditionally they had taken a hands-off approach, preferring to make their profits by working with the already public, multimillion dollar top firms.

But suddenly profits from this source began drying up. Due to regulatory changes allowing shelf-registrations, mega-corporations can now put their own financing deals together. They no longer require the financial institutions' help in forming syndicates.

As a result, the bankers had to sit down and do some strategic planning to determine how they could replace those profits. They looked at the typical underwriter discount of 7%, saw it as profit free and clear and started falling all over themselves trying to get that business. They provided the mechanism that was needed for companies to go public.

The response of numerous private companies to the unexpected convergence of these three factors was predictable—they rushed into the market.

Among retail IPOs, some of these entries were hastily formed new companies that almost instantaneously went public to obtain expansion capital. Most of the computer chains went this route. For example, San Jose, Calif.-based Businessland currently has 14 retail units. But having gone public in December 1983, it expects to be able to finance 35 more stores by the end of 1984 (*Chain Store Age Executive*, December 1983).

The strong market for IPOs also afforded would-be entrepreneurs the opportunity to leave established retail companies and to strike out on their own. Among retailers, the chief example during 1983 was Frank Denny, formerly head of W. R. Grace's mammoth home center operation. He left that company in March to join a group of investors in the creation of Home Centers of America. The company went public in May and has been busy opening Home Pro warehouse stores ever since. (It has also made money for its investors. The stock was initially offered at $6.25 per share; by the end of the year the price had more than quadrupled to approximately $27 per share.)

Another example is Gene Ferkauf, best known as the founder of Korvettes. Back for a second round, last year he formed the ClubMart of America operation. The company went public in May and in December opened its first store in New York City, modeled on the wholesale warehouse club concept. (So far Ferkauf's operation hasn't fared too well on Wall Street. The stock was initially offered at $5.25 a share; as of Dec. 21, it was selling for $5 a share.)

Yet by far, the single largest group of IPOs in the retail industry made in 1983 came from established retail chains—grabbing hold of the opportunity to go public at last.

For Farm Fresh, the Norfolk, Va.-based supermarket chain that was the first retail operation to take advantage of this window when it went public last March, the timing couldn't have been better.

Over the last five years the company had been increasing sales at the rate of 25% annually; earnings at the rate of 39%. This has been accomplished through the renovation of its stores to make them larger and to test and develop the company's combo-store concept.

The finalization of this concept coincided with the opportunity to come to market to obtain financing for a rather ambitious expansion program. In 1982, space increased by only 4%; in 1983 it was up 34% with the opening of four stores; it is expected to rise 42% this year with six new stores in the works.

More typical than Farm Fresh's situation is the established company that goes public to add to the personal worth of the founder (often financing expansion is another, but somewhat less important, reason). An example is Merry-Go-Round which operates both women's and men's apparel stores and which went public in July.

"Our major reason for going public was that except for taking a modest salary, our two principal shareholders who had built the business over the past 12 or 13 years had never developed an estate. We felt that they should have a vehicle to make that happen," explains Michael Sullivan, Merry-Go-Round's president. (Plans to go public were actually initially made in 1973—before the first oil embargo sent retail stocks plummeting.)

An additional benefit is that being public "gives the company officers and other people in the organization a way to participate on an equity basis in the growth of the company. We felt that this was critical—especially for a company that has grown from two stores in the early 1970's to 225 stores at the end of 1983 and with plans this year to open 40 to 45." (Sullivan emphasizes that none of the capital raised through the IPO is being used for this expansion.)

Other examples of companies that went public for the enrichment of their founders' portfolios include:

- Dress Barn, which through its public offering last May made approximately $17 million for Elliott S. Jaffe, president, and his family who retained 47.5% of the company.
- Burlington Coat Factory, which raised $66 million when it went public in June, $44 million of which went directly into estate trusts of the Millstein family. The family still owns 65.22% of the company.
- Syms, where founder Sy Syms Merns, by selling approximately three million newly issued shares of stock in September made himself about $44 million as part of a $51 million IPO.

However, to claim that these companies go public simply for the enrichment of the founders is an oversimplification. At Dress Barn, for example, going public represented more than "a chance for the principals to get some money out of the business," points out Michael Palmer, vp-finance.

"Even more importantly, we were able to solidify our financial position. We were able to put enough money

into our treasury so that now we can weather any type of storm. (*For the reaction of Monroe Millstein, president of Burlington Coat Factory, see related story.*)

Palmer admits that "Going public was a real ego thing for everybody involved." More significantly, "We can now make stock offers to employees and that attracts better employees. It is just like companies that offer Blue Cross and other such benefits. We have to offer them too."

He adds that "By going public, we've gone from being a little company to being a first class operation."

Yet, following this route "definitely changes the personality of a company. For the chief executive, it means not only having to devote some of his time to meetings with the financial community, but learning to deal with the decision-making constraints, real or imagined, imposed by both stockholders and the investment community.

"When a company is private, the owner is his own boss. If he comes up with a five year plan that requires feeding a lot of retained earnings back

1983 retail IPOs

Company	Type of store/ retailer	Date public	Price	P/E	P/E 12/21/83	% change	Price 12/21/83	% change
Farm Fresh	Supermarket	3/25/83	$16.33	23.1	25.3	9.5	$19.25	17.9
Devon Stores	Hard goods	4/5/83	13.33	20.2	15.2	−24.8	12.00	−10.0
Deb Shops	Women's apparel	4/6/83	17.50	16.4	14.5	−11.6	20.50	17.1
Trak Auto	Auto supplies	4/26/83	22.00	21.6	18.2	−15.7	16.00	−27.3
E&B Marine	Marine supplies	4/27/83	12.00	14.8	20.3	37.2	20.75	72.9
Dress Barn	Off-price apparel	5/4/83	23.00	37.1	23.7	−36.1	22.00	− 4.3
CompuShop	Computers	5/12/83	8.00	34.8	22.9	−34.2	11.00	37.5
Home Centers of America	Bldg. supplies warehouse	5/13/83	6.25	NM	NM	NM	9.00	44.0
Computer Factory	Computers	5/17/83	12.50	39.1	22.9	−41.4	8.00	−36.0
ClubMart of America	Membership off-price	5/18/83	5.25	NM	NM	NM	5.00	− 4.8
Vitality Unlimited	Health food	6/1/83	7.75	NM	NM	NM	4.38	−43.5
Burlington Coat	Off-price apparel	6/9/83	28.00	26.4	19.4	−26.5	21.75	−22.3
Merry-Go-Round	Apparel	7/6/83	21.00	21.9	16.8	−23.3	22.00	4.8
Williams-Sonoma	Mail order	7/7/83	23.00	31.9	22.3	−30.1	14.50	−37.0
Convenient Food Mart	Convenience foods	8/2/83	10.00	13.7	10.1	−26.3	7.50	−25.0
Crown Books	Books	8/9/83	25.00	48.1	27.6	−42.6	18.75	−25.0
Shoe Town	Off-price shoes	8/31/83	10.00	NM	NM	NM	9.88	− 1.3
Comp-U-Card	Computer service	9/15/83	20.50	NM	NM	NM	23.00	12.2
Pearle Health Services	Optical	9/16/83	17.00	14.4	16.0	11.1	20.63	21.3
Syms	Off-price apparel	9/23/83	15.00	28.8	28.2	− 2.1	15.25	1.7
National Lumber & Supply	Building supplies	10/4/83	10.00	20.8	17.4	−16.3	9.75	− 2.5
Designhouse International	Furniture	10/6/83	10.50	12.4	14.4	16.1	12.25	16.7
Casey's General Stores	Convenience stores	10/20/83	15.00	17.2	12.2	−29.1	10.50	−30.0
Parisian	Apparel	11/10/83	14.50	15.1	15.8	4.6	16.13	11.2
The Federated Group	Electronics	11/15/83	12.50	18.9	17.5	− 7.4	15.75	26.0
Rent-A-Center	Hard goods	11/21/83	14.50	22.7	20.8	− 8.4	13.75	− 5.2
CML Group	Apparel	11/22/83	13.00	13.3	13.3	0.0	13.00	0.0
Medicare-Glaser	Pharmacy	11/23/83	8.00	—	19.0	—	8.00	—
Delchamps	Supermarket	11/25/83	14.00	11.6	9.6	−17.2	11.63	−17.0
The Computer Store	Computers	11/30/83	6.00	NM	NM	NM	0.94	−84.4
Mars Stores	Discount dept.	12/2/83	5.75	10.1	11.0	8.9	6.25	8.7
Entre Computer Centers	Computers	12/6/83	12.00	171.4	86.8	−49.4	14.75	22.9
Clothestime	Off-price apparel	12/9/83	11.00	20.4	18.1	−11.3	9.75	−11.4
Businessland	Computers	12/15/83	10.00	—	—	—	10.13	—
Medicine Shoppe Int'l	Pharmacy	12/19/83	12.50	—	—	—	13.75	—
Dwight Health Care	Dental care centers	—	—	—	—	—	—	—
Royal Int'l	Optical	—	—	—	—	—	—	—

NM—Not Meaningful
Source: Daniel Barry, Kidder, Peabody & Co.

into an ambitious expansion, using money that would otherwise provide a nice cash surplus, he can do this. But when the company is public, that's not always the case."

The potential for conflicts is always present because of the fact that "Investors and analysts live on quarterly numbers. They typically expect to see substantial earnings per share growth on an annual basis. When it doesn't appear, they can become nasty, asking a lot of questions, making a lot of telephone calls and wondering aloud why the stock plummeted. This can't help but become a factor in decision-making."

Mitchell Rubinson, president of Cache, a women's apparel chain that went public approximately two and a half years ago, admits that, "As a private company, I used to think about what I wanted to do in a year, in five years and as the ultimate goal. As a public company I think exactly the same way—but I do worry more about the individual fiscal quarters because the investment community, particularly security analysts, place a lot of importance on those results. Sometimes this creates a lot of pressure, but I try not to let it affect me."

He adds that "After you go public, you have to communicate more, you have to answer questions and you have to be more responsive—even if you own the lion's share of the business. You are no longer a private person."

At Merry-Go-Round, Sullivan acknowledges that "We do now report things that we did not report in the past and we have to discuss our performance in greater detail, but I haven't been reluctant to do that. We have done so well in our past few quarters it's been a pleasure to tell. But, if we were in a different position, this might change."

The companies that joined Merry-Go-Round in going public last year were able to take advantage of market conditions for IPOs that, at least for retail offerings, may no longer exist.

The chief reason, according to Daniel Barry, a retail industry analyst with Kidder, Peabody & Co., is that at least through the first half of this year, "Retail stocks are expected to underperform the market and to be down on an absolute basis." He expects apparel-related companies to be particularly hard-hit.

"This means that the window of opportunity for retail chains going public is shut except for a very few exceptional companies," he claims.

That may spell bad news—particularly for the seven retail companies that still had preliminary filings for IPOs pending at the end of 1983. ■

—Jacquelyn Bivins

INTERVIEW

Public image wearing well at Burlington Coat Factory

"Being public is great fun now. But, if the figures were bad I probably wouldn't be finding it so much fun." *—Millstein*

By going public, "we became masters of our own destiny," says Monroe G. Millstein, president and ceo of Burlington Coat Factory.

The company, which went public on June 9, 1983, is one of the acknowledged leaders among off-price apparel chains. Yet, although it has been in the retail business for over a decade (and in the wholesale business since 1924), it wasn't until corporate suitors came along that the Millstein family thought about taking the company public.

With the business growing swiftly, Millstein recalls that early in 1983, "We were approached by several giant companies who wished to acquire us. They asked for us to project our five-year plan—something we had never really done before. Once it was completed, we saw that we would have no problem carrying it out ourselves. By going public we were able to get the capital to expand."

As a further incentive, Millstein observes that "I had been told by executives of other companies that had been acquired that no matter what they were told ahead of time, it was not the same after they sold out."

Yet, despite the advantages Millstein sees in having gone public (including the $44 million that went to the Millstein family), he admits that "everybody has become a critic."

He enjoys telling the story of the young institutional investor "who, after visiting one of our stores back in July, told me that we were wrong in claiming that we are appealing to an upscale consumer. He said we were going after the K mart customer. This comment came after he and his wife hadn't found anything they wanted. Yet, he and his wife returned to the same store in November and this time they spent $600. He then said to me, 'Hey, you changed the merchandise mix, didn't you?' But we didn't—the store had the same brands. What happened was the first time he came in he wasn't ready for what we were doing. We now have lots of those critics and judges."

Millstein is also coming to realize that it's impossible to please everyone. For example, "Recently, one of our investment advisers said to me, 'I like your company. I particularly like the fact that you don't have a financial public relations firm.' But then I told him that because of the recommendations of other people 'I just hired one—he wants me to talk at meetings.' The response of the adviser was 'but I want you to stay home and run the business. That's why I invested in your company' " (Millstein estimates that so far only about four hours of his time a week are being spent on responsibilities specifically attributable to now being a public firm.)

Despite the critics, with Burlington Coat continuing to generate sizable sales and profit increases, Millstein says that "Being public is great fun now. But, if the figures were bad I probably wouldn't be finding it so much fun." ■